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Policy Considerations for Enhancing Student Access and Persistence in a World in Which Tuition Keeps Rising

by

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I. Introduction

The United States no longer leads the world in college completion rates. Inequality in college access rates by income have barely narrowed over the last 25 to 30 years and inequality in college completion rates have narrowed even less. The groups in the population that are growing the most rapidly are those that have historically been underrepresented in higher education. What types of federal policies might help to address these issues in the face of tuition levels at private colleges and universities that have risen for over a century by an average of 2 to 3.5 percent a year more than the rate of inflation and tuition levels at public colleges and university that have recently risen at similar rates. And why does tuition keep rising and can anything be done about that?

Improving undergraduate access and persistence through to graduation is not the only goal for higher education policy. We should seek to improve, or at least maintain, the quality of higher education. We should also remember that higher education is much more than undergraduate education. The scientific research that goes on at research universities is essential for our nation's economic well-being. So too are the doctoral students who contribute to the production of research and become the next generation of college faculty and researchers. Finally, there is the role of land grant universities specifically, and public higher education more generally, in improving the welfare of the population beyond their enrolled students through extension and outreach activities.

Public policies that affect any of these other aspects of higher education will inevitably influence the ability of academic institutions to improve access and persistence. For example, over the last 25 to 30 years the share of the ever expanding research budgets at America's research universities financed out of institutional funds (such as

endowment income and annual giving) has increased. A recent Congressional proposal to cap indirect cost reimbursement rates at 35% on basic-research grants and contracts financed by the Defense Department would further shift the costs of funding research onto the universities, leaving them with fewer resources to provide grant aid for students and/or putting more pressure on their tuition levels.

II. Private Higher Education

Two-thirds of all four-year college students are enrolled in public higher education institutions; this share rises to four-fifths if we include two-year college students. Hence, public concern over issues of cost, access and persistence really should be directed towards this sector. However, because tuition levels at the high priced selective private institutions receive so much attention, I begin my discussion with them.

The factors that have led to continual tuition increases at these institutions are described in detail in my book *Tuition Rising*. They include the failure of faculty productivity in teaching to grow substantially; the quest by institution to be the very best that they can in every dimension of their activities which has led to an arms race of spending; the widening distribution of earnings in the United States which creates pressure on students and their families to “buy the best” and leads to an increase in the numbers of students applying to the selective privates, thereby reducing any competitive pressure that might moderate tuition increases; and the *U.S News & World Report* annual ranking of colleges and universities that reward institutions for increasing spending. In private higher education, increases in tuition are almost always associated with increases in educational expenditures per student.

Tuition increases at private colleges and universities overstate the increase in costs faced by students because tuition discounting is increasingly prevalent. Recent surveys by the National Association of College and University Business Officers and the College Board suggest that the typical private college or university gives back 30 to 40% of its tuition revenue to students in the form of grant aid. However, increasingly this aid is “merit” rather than “need” based as institutions increasingly use aid to “craft their classes” rather than to ensure access and persistence. Today, there are only a few institutions, such as my own, that provide only need based financial aid.

While their tuitions continue to increase, the endowments at the richest private colleges and universities have also soared. In 2005-2006 the wealthiest 10 percent of private colleges and universities had about \$450,000 in endowment per student, while the median private institution had only about \$15,000. Disparities in endowment wealth are enormous even among those in the upper tail of the endowment distribution. For example, in June 2006 Princeton’s endowment per student was about 8 ½ times Cornell’s.

Why should policy makers care about simultaneous high tuition and high endowment levels at wealthy selective private colleges and universities? After all, no student is forced to attend them. The answer is that research shows that students who attend institutions that spend more educating them have higher post college earnings and greater probabilities of going to graduate and professional schools. Taxpayers as a whole subsidize these institutions through the favorable tax treatment they receive (no taxes on endowment income, tax deductions for the contributions made to them, exemption from local property taxes, and ability to issue tax free bonds). In return for this favorable tax

treatment, these institutions are expected to act in the public interest; one aspect of this is for them to remain accessible to students from all family income levels.

Currently the proportion of Pell Grant recipients at many of them is far below the proportion of Pell Grant recipients among students nationwide. While there are many reasons for this, including inequities in our nation's public elementary and secondary education system (often based upon family income) that limit the ability of students from lower income families to compete for positions at selective institutions, the wealthiest privates have understood their responsibilities and embarked on programs to enhance enrollments of students from disadvantaged families- by drastically improving financial aid packages, aggressively recruiting students, and providing enhanced support for those who enroll. However, the disparities in endowment wealth, even in the upper tail of the private institution endowment distribution, make it unlikely that the vast majority of private academic institutions could pursue similar policies.

What about proposals to require academic institutions to have minimum spending rates from their endowments of 5% in the hope this would force them to spend more on financial aid? These proposals appropriately assume that the average rate of return on endowment assets will be sufficiently high that a 5% spending rate will still enable an institution to maintain the real value of its endowments over time. Most institutions base endowment spending decisions on an average value of their endowments over a number (often 12) quarters and their spending rates from this average currently are below 5%.

Endowments are not analogous to savings accounts; they often are legally restricted to specific uses (e.g. an endowed professorship) and the distributions they generate can't always be used for financial aid. However, many activities that endowments support are

not fully funded by spending from them and require support from the institution's general operating budgets. Generating extra spending from an endowment will often free up funds from the general operating budget of a private institution that can then be used for financial aid. Private academic institutions should be held accountable for the tax benefits they receive and requiring a minimum spending rate of 5% of the average value of their endowments over a three year period is a reasonable way to both increase accountability and generate some additional institutional funds that could be used for financial aid.

III. Public Higher Education

During the last 25 to 30 years tuition increases at four-year public institutions have been slightly higher in percentage terms than tuition increases at four-year private institutions. However, the dollar increases have been smaller at the publics, so in real terms the dollar gap between public and private tuition has increased. Tuition increases at the publics have been driven largely by the failure of state support per student to grow much in real terms; it has been essentially flat if one uses the Higher Education Price Index (HEPI) rather than the CPI. In contrast to what goes on in private higher education, in years when state support is cut, tuition increases in public higher education often are associated with decreases in expenditures per student.

As a result expenditures per student in public higher education have fallen relative to expenditure per student in private higher education, leading to declining relative salaries of faculty in public institutions (making it increasingly difficult for the publics to attract and retain top faculty) and to an increased use of part-time and full-time non tenure-track faculty (which research shows is associated with a reduction in graduation rates). Put

simply, there is no such thing as a free lunch and inadequate funding for public higher education is having serious impacts on the quality of these institutions.

Educational expenditures per student vary widely across types of public higher education institutions; they are larger at the flagship doctoral institutions than they are at the comprehensive (masters') institutions and larger at the latter than they are at the two-year colleges. Conversely, the proportions of students who are Pell Grant recipients are larger at the two-year colleges than they are at the comprehensives, which in turn are larger than they are at the flagship doctoral institutions. Inasmuch as higher expenditures per student are associated with higher post college earnings, on balance the income gains that students get from attending college are positively related to their initial family income levels. This disparity in expenditures per students received by students from different family income levels is amplified by the changing distribution of financial aid programs; increasingly state grant aid programs are merit rather than needs based and the expansion of federal subsidized loan and tax credit programs benefits primarily middle- and upper-middle-income students rather than students from lower-income families.

The privatization of public higher education that is occurring (moving towards further reductions in state support and allowing public institutions more freedom to raise their tuitions) is most likely to be successful at the flagship doctoral institutions. Students' demand for places at them will allow them to raise tuition and still fill all their seats, while their substantial endowments and ability to generate large annual giving streams can them help fund institutional financial aid to maintain access. The comprehensives and two-year colleges face much less favorable conditions and privatization of them will likely price some students, primarily those from lower-income families, out of college.

To improve access and persistence, policies need to be developed to get more students from lower-income families to the flagship doctoral institutions and to encourage states to spend more on their higher education systems and to limit tuition increases at the comprehensives and two-year colleges. A number of flagship public doctoral institutions have developed programs similar to those at the wealthiest privates to increase access and persistence of students; examples include Access UVA, the Carolina Covenant and the Texas Longhorn Opportunity Scholarship Program.

Approximately 40 percent of all first-time freshmen begin their studies at two-year colleges, with about 90 percent of these starting at public colleges. The transitions from two-year colleges, where many students from lower-income families begin, to four-year colleges are often not seamless and hinder the students' progression to four-year degrees. While many problems in this area need to be addressed at the state level, federal policies ought to provide incentives for institutions and states to facilitate these transitions.

Research suggests that there is at best a very weak relationship between the amount that a state spends on its public higher education system and the fraction of its population that has a college degree. This should not be surprising, because college educated workers can move across state lines to where job opportunities are the best. However, this lack of a strong relationship between state spending on higher education and the education level of the state's work force provides an incentive for states to invest less than is socially optimal in higher education. Inasmuch as the nation as a whole benefits from a highly educated workforce, this provides another reason for the desirability of the federal government providing incentives for states to invest more in higher education.

IV. Federal Policy Recommendations

How the federal government finances Medicaid and the Pell Grant program is asymmetrical. When a state spends more on Medicaid, it gets more federal matching funds. In contrast, historically, when a state spent less on its higher education system and a public higher education institution responded by raising its tuition, the higher tuition increased the amount of Pell Grant funding that some residents of the state were eligible for because Pell Grant award levels were limited by the tuition that students paid. Thus states received more federal funds if they increased Medicaid funding, but less federal funds if they increased state funding for higher education (which allowed tuition levels to be kept low). The Budget Reconciliation Bill (HR2669) of 2007, which permanently repealed the tuition sensitivity provision in the Pell Grant program, was a step in the right direction; it removed the incentive states had to cut back their funding of their public higher education institutions, but it did not provide any incentive for them to spend more. The College Opportunity and Affordability Act of 2007 begins to provide such incentives.

If the increased enrollment and persistence of students from lower-income families is a policy goal, federal funding policies should support this objective. Another way to achieve this would be to base the federal SEOG funding that goes to institutions on the volume of Pell Grant funds that their students receive, not on historical entitlements. Expanding the size of a restructured SEOG program would provide both public and private institutions with more discretionary funds to allocate for need based financial aid.

Of course critics of governmental grant aid programs often argue that when grant aid programs are expanded, institutions try to capture the increased aid by increasing their tuition, which reduces the chance that the program actually will lead to increased

enrollment and persistence of students from lower-income families. In the main, academic research does not find that this occurs. However, the possibility raises the issue of whether governmental efforts to expand access and persistence should also seek to provide incentives to academic institutions to accomplish these goals.

One possible policy would provide funding to each two- and four-year institution based on the numbers of Pell Grant recipients enrolled at the institution, or the dollar volume of Pell Grant program funds its students receive. In addition, to encourage persistence, additional funding would be provided for each two-year, or four-year degree granted by the institution to Pell Grant recipients. Institutions would be free to use these funds in any way that they saw fit; they might use them for institutional aid, for support services to enhance persistence, or for recruitment of students. Each institution could choose allocate the funds in ways that benefited it the most. Such a policy was actually part of the original Pell Grant proposal in 1972, although it was never enacted. It recognizes the additional costs that institutions face in recruiting and educating through to graduation students from lower-income families and it provides a financial incentive to encourage institutions to expand their enrollments and graduation rates of these students.

Given that the vast majority of students from lower-income families are enrolled at public comprehensives, public two-year colleges, and less well-endowed private four - year colleges, such a program would benefit most those institutions. Note that because four-year colleges would receive funds for each Pell Grant recipient that they graduate, they would have an increased incentive to enroll Pell Grant recipients transferring from two-year colleges; they would bear the cost of educating these students for only two years, but receive the same “reward” that they would receive for graduating Pell Grant

recipients who initially enrolled as freshmen. For many years New York State has had a Bundy Aid program which provides grants to private colleges and universities in the state for each degree that they award to state residents. Its private four-year colleges have taken advantage of the program's incentives and aggressively recruit graduates of New York's public two-year colleges.

Space constraints prevent me from discussing in detail a number of other policy issues Congress might consider, but I will mention two briefly. The financial aid system needs to be simplified and made more transparent. Students need to know about their Pell Grant eligibility, their prospective funding level and what the costs of attending colleges in their state would be well in advance of their senior year of college. Given the variation in state grant aid programs, it would be important to work towards an integrated system in which students would learn about their eligibility for and potential size of state grant aid at the same time.

Finally, proposals to penalize academic institutions for raising their tuition levels more than a certain rate should be viewed with caution. The lower an institution's tuition, the smaller the increase in revenue that it receives for any given percentage increase; so large percentage tuition increases at public institutions often generate less revenue per student than smaller percentage increases at private institutions. Tuition increases in public higher education often are efforts to (partially) make up for cuts in states support. Tuition increase in private higher education often are a result of efforts to maintain or increase quality and part of the tuition increases are used to generate funds for grant aid. Rather than focusing on tuition levels and increases, policy should focus on whether academic institutions are maintaining and expanding access and persistence.

